INTERACTIONS AMONG PROGRAMS PROVIDING BENEFITS TO INDIVIDUALS: SECONDARY EFFECTS ON THE BUDGET

The Congress of the United States
Congressional Budget Office

NOTES

Unless otherwise indicated, all years referred to in this report are fiscal years.

Details in the text and tables of this report may not add to totals because of rounding.

PREFACE

Reductions in programs that provide benefits to individuals often produce large offsetting increases and decreases in spending by other programs. These offsets have important, differential effects on federal and state budgets as well as on the individuals affected. This report, prepared at the request of the Senate Budget Committee, estimates these interaction effects for two general options to achieve spending reductions: an across-the-board benefit reduction and an eligibility restriction. In keeping with the Congressional Budget Office's (CBO) mandate to provide objective and impartial analysis, this study contains no recommendations.

Reuben Snipper, of CBO's Human Resources and Community Development Division, prepared the paper under the supervision of Paul B. Ginsburg and Nancy M. Gordon. The author wishes to acknowledge the technical and critical contributions of many people, particularly Roger Hitchner, Charles Seagrave, Thomas Buchberger, Paul Cullinan, Daniel Koretz, Ben Steffen, Howard Levine, Patricia Ruggles, and Bruce Vavrichek. Patricia H. Johnston edited the manuscript. Reba Williams typed the many drafts and prepared the paper for publication.

Alice M. Rivlin
Director

May 1982

CONTENTS

TABLES

PAGE

TABLES

PAGE

APPENDIX TABLE

PAGE

SUMMARY

Last year's budget decisions reduced substantially federal spending in fiscal year 1982 for programs that provide benefits to individuals. For fiscal year 1983, the Administration has proposed more large cuts for such programs. A reduction in one of these programs often results in increases or decreases in benefits provided by other programs, making the net impact on the budget, and on the affected individuals, significantly different from the initial effect of the cut program.

PROGRAMS THAT PROVIDE BENEFITS TO INDIVIDUALS

Programs that provide benefits to individuals are conventionally divided into social insurance or welfare categories. Social insurance programs furnish benefits to persons with a particular characteristic--aged, unemployed, or disabled, for example--who usually have contributed to the program's support, often through earmarked taxes and with employer contributions. Generally, neither eligibility nor benefits depend on the income or assets of the beneficiary. Social insurance programs included in this study are Social Security, unemployment insurance, and Medicare.

Welfare programs, in contrast, take account of the income and assets of recipients in determining eligibility and benefit amounts, but do not condition eligibility on prior contributions. For this reason, they are referred to as "means-tested" programs. The welfare programs analyzed here--Aid to Families with Dependent Children (AFDC), Supplemental Security Income (SSI), food stamps, school lunch, housing assistance, and Medicaid--provide cash and in-kind assistance to those meeting specific definitions of need.

PROGRAM INTERACTIONS

Program interactions occur because many people participate in more than one program and because benefits in some programs depend on benefits received from others. The extent to which individuals participate in more than one program depends on the eligibility rules, benefit formulas, and program regulations for the particular programs involved. In a few cases, participation in one

program makes individuals automatically eligible for benefits in another--Medicaid eligibility is given to all AFDC and most SSI recipients, for instance. More generally, several programs share the same general eligibility requirement--low income--because they were designed to meet different needs of the poor. For example, the food stamps, AFDC, SSI, and Medicaid programs all have income limits, although the last three have additional requirements as well. Consequently, many poor families receive benefits from more than one of these programs.

Because benefit formulas and program regulations in welfare programs count cash payments from other programs as income, reductions in the benefit levels of one program often result in partially offsetting increases in benefits paid by other programs. For example, AFDC cash assistance is counted as income in figuring food stamp benefits. Thus, for the 75 percent of AFDC families who participate in the Food Stamp Program, roughly one-third of a decline in AFDC benefits would be offset by increased food stamps. On the other hand, when eligibility for two programs is linked, as in AFDC and Medicaid, loss of benefits from one can mean loss of benefits from the other.

This report estimates the net effect on government spending and household benefits of reductions in three major programs--AFDC, Social Security, and unemployment insurance (UI). These programs assist primarily low-income, single-parent families, elderly persons, and unemployed workers--the major groups served by programs providing benefits to individuals. The study examines the implications of benefit changes in these three programs for six other programs--Supplemental Security Income, food stamps, school lunch, housing assistance, Medicare, and Medicaid.

EFFECTS OF PROGRAM REDUCTIONS ON FEDERAL SPENDING

In order to illustrate program interactions, this report analyzes two options designed to achieve a hypothetical 20 percent reduction in spending in AFDC, Social Security, and unemployment insurance:[1]

- An across-the-board benefit reduction, and
- A restriction in eligibility.

1. This large reduction was used so that the smaller interactions would appear in the estimates.

Over half the reduction in federal spending resulting from an across-the-board benefit cut in AFDC would be offset by increased spending for other programs (see Summary Table 1). In particular, a 20 percent across-the-board reduction in AFDC benefits would produce federal budgetary savings of about 9 percent, if offsets by other programs were included. This large interaction would occur because of extensive participation by AFDC recipients in other federal programs and because of the way costs are shared among federal, state, and local governments. The federal government would pay all the increased costs in food stamps and housing assistance programs but reap only about half the overall savings from cutting AFDC; state and local governments would receive the other half.

SUMMARY TABLE 1. INTERACTION EFFECTS ON THE FEDERAL BUDGET OF AN ILLUSTRATIVE 20 PERCENT REDUCTION IN SPENDING IN THREE PROGRAMS IN FISCAL YEAR 1983, BY TYPE OF REDUCTION

Cut Program by Type of Reduction	Offset to Each Dollar Cut from Program (In cents)	Net Cut as Percent of Previous Program Outlays, Including Offsets
Benefit Reduction		
AFDC[a]	55	9
Social Security[b]	7	19
Unemployment Insurance	3	19
Eligibility Restriction		
AFDC[a]	5	19
Social Security[b]	1	20[c]
Unemployment Insurance	3	19

SOURCE: CBO estimates.

a. Aid to Families with Dependent Children.
b. The term Social Security is used here to include both Old Age, Survivors, and Disability Insurance (OASDI) and Railroad Retirement programs.
c. The offsets are small enough that the net cut rounds to 20 percent.

In contrast, an across-the-board reduction in Social Security or unemployment insurance benefits would not be offset significantly by increased costs in other programs. A 20 percent cut would generate net federal savings of about 19 percent in Social Security and unemployment insurance, when increases in other programs are taken into account. Unlike recipients of AFDC, Social Security and UI beneficiaries are generally not eligible for means-tested programs.

The eligibility restrictions used in this report to reduce spending in AFDC and Social Security would produce smaller federal offsetting increases in other programs than would be the case for the across-the-board benefit reduction. For example, each dollar cut in AFDC by the eligibility restriction would be offset by 5 percent, as compared to 55 percent for the across-the-board benefit reduction. Similarly in Social Security, the eligibility restriction would be offset by only 1 percent, as compared to 7 percent for the benefit reduction. The smaller degree of offsetting changes would occur for two reasons. First, fewer people who would be affected by the eligibility restriction participate in other programs. Second, loss of Medicaid or Medicare benefits would produce additional savings, since eligibility for the health-care programs is linked to eligibility for AFDC and Social Security, but not to the level of benefits.

For unemployment insurance, both the eligibility restriction and the across-the-board benefit reduction would increase federal spending in other programs by the same amount--about 3 percent of the UI cut. In each case, the effects on other programs would be similar.

EFFECTS OF PROGRAM REDUCTIONS ON STATES AND INDIVIDUALS

Changes in state and local government spending resulting from either benefit reductions or eligibility restrictions could be quite different from the federal pattern, because of the way program costs are shared among different levels of government. For instance, state and local governments would derive their full share of a benefit reduction in AFDC, but would pay none of the offsetting increases in food stamps or housing assistance (see Summary Table 2). More striking, for a 20 percent eligibility restriction in AFDC, the net decline in state spending would be 23 percent, on average, because of additional savings associated with the loss of Medicaid eligibility for some recipients. In contrast, cutting Social Security would not reduce state spending

SUMMARY TABLE 2. INTERACTION EFFECTS ON STATE AND LOCAL BUDGETS OF AN ILLUSTRATIVE 20 PERCENT REDUCTION IN SPENDING IN THREE PROGRAMS IN FISCAL YEAR 1983, BY TYPE OF REDUCTION

Cut Program by Type of Reduction	Offset to Each Dollar Cut from Program (In cents)	Net Cut as Percent of Previous Program Outlays, Including Offsets
Benefit Reduction		
AFDC[a]	0	20
Social Security[b]	0	c
Unemployment Insurance	0	0
Eligibility Restriction		
AFDC[a]	-14	23
Social Security[b]	1	c
Unemployment Insurance	0	0

SOURCE: CBO estimates.

a. Aid to Families with Dependent Children.

b. The term Social Security is used here to include both Old Age, Survivors, and Disability Insurance (OASDI) and Railroad Retirement programs.

c. State spending would increase, not decrease, because of additional spending for SSI and Medicaid. Since states pay none of the Social Security benefits, a percentage cannot be calculated.

because states do not share in financing Social Security; instead, state spending for SSI and Medicaid would increase by about 1 percent of the reduction in Social Security outlays. For unemployment insurance, states would neither benefit from reduced spending nor pay any offsetting increases in other programs.

Effects of program reductions on individual families would depend on the size of the change and the exact pattern of program participation. For the three-quarters of AFDC recipients who also participate in food stamps, about one-third of their loss of AFDC benefits would be offset. One-fifth of AFDC families who receive some type of housing assistance would pay less rent if their AFDC benefits were reduced or ended; therefore, they would be partially cushioned from the full effects of an AFDC cutback. Overall, because of participation in programs that would partially offset an AFDC cut, less than 20 percent of AFDC households would experience the full reduction in benefits. In contrast, far fewer beneficiaries of Social Security and unemployment insurance participate in programs that would offset reductions, so more than 80 percent of them would face the full drop in benefits from changes in those programs.

CHAPTER I. INTRODUCTION

About half of the federal budget is spent on programs providing benefits to individuals. Legislation enacted in 1981 cut over $13 billion in fiscal year 1982 outlays for these programs from the $366 billion projected under the Congressional Budget Office's (CBO) current policy assumptions. The President's budget for fiscal year 1983 proposes additional reductions of a similar size for many of these same programs.

Some of the people affected by these budget cuts participate in more than one benefit program. For those who do, a cutback in benefits in one program may increase or decrease benefits in another. If enough people participate in more than one program, the net impact on the federal budget could be significantly different from the initial reduction in outlays for the affected program. These offsetting increases or decreases in spending by other programs are called program interactions or secondary budget effects.

Program interactions not only affect the net budgetary impact of program changes, but they also alter the effects of the cuts on the individual households receiving benefits. In some cases, benefits from other programs automatically increase, thus partly reducing the impact. In other cases, however, loss of eligibility for one program leads to loss of eligibility in others, thereby magnifying the effects.

Individuals whose benefits are reduced are likely to alter their behavior in ways that have further effects on the budget. For example, their likelihood of working or the amount they work might change, and they might spend less. These changes would, in turn, affect the aggregate level of economic activity and, ultimately, tax receipts and spending in other programs. While these "feedback effects" all affect the budget, they are not discussed in this report, which focuses only on the direct effects and interactions of program changes.[1]

---

1. For a discussion of feedback effects in the economy and on the budget, see Congressional Budget Office, How Changes in Fiscal Policy Affect the Budget: The Feedback Issue (May 1982).

94-308 0 - 82 - 3

PLAN OF THE PAPER

This report analyzes the interactions among major programs that provide benefits to individuals. (See Appendix A for a description of these programs.) Chapter II explains how and why interactions occur and describes the major ones. Chapter III provides estimates of the interactions produced by cutting three programs--Aid to Families with Dependent Children (AFDC), Social Security, and unemployment insurance. In each of these programs two kinds of cuts are considered: an across-the-board benefit reduction and a restriction in eligibility. Effects on federal and state budgets are discussed, as well as effects on individual households. Finally, several current proposals to reduce spending in AFDC and Social Security are examined.

CHAPTER II. HOW THE PROGRAMS INTERACT

Of all households participating in major federal programs that provide benefits to individuals, over half receive assistance from two or more programs. Since benefits in one program often depend partially on benefits in another, changes in one program create the potential for large secondary effects on the budget.

This chapter discusses what these secondary budget effects are, explains how and why they occur, and provides estimates of the multiple program participation that chiefly determines the magnitudes of the interactions. The analysis focuses on cutbacks in three major programs--Aid to Families with Dependent Children (AFDC), Social Security, and unemployment insurance (UI)--that interact with six other programs--food stamps, Supplemental Security Income (SSI), housing assistance, school lunch, Medicaid, and Medicare. The people participating in these programs--single-parent families, the elderly, and the unemployed--represent the major groups served by the entire income security system.[1]

MECHANISMS OF PROGRAM INTERACTIONS

For interactions to occur, beneficiaries of one program must participate in another[2] and the benefits in the second program must be affected by either participation in or the level of benefits from the first. The essential element beyond multiple participation is that benefits in one program depend on benefits in another.

Beneficiaries generally participate in more than one program because several federal programs are designed to serve different

---

1. Other vulnerable groups not included in this study are the disabled, the sick, and veterans, but even some of them are served by the nine programs covered in this report.

2. For convenience throughout this paper, the analyses of program participation are discussed in terms of current participants. The analyses, in fact, pertain both to these households and to similar households not currently participating in the programs.

needs of people in similar circumstances. For example, food stamps and AFDC both assist low-income families, resulting in a high degree of overlapping participation. In a few cases, program rules in one program automatically qualify participants for eligibility in another. Households eligible for AFDC are categorically eligible for Medicaid, for instance. Moreover, households may participate in more than one program because individual members qualify for different programs or because the entire household is eligible for more than one program.

Multiple participation, by itself, does not necessarily cause interaction, because programs only interact when benefits in one program affect benefits in another. In general, means-tested programs are more likely to interact than social insurance programs, since benefits from programs such as SSI and food stamps are affected by the amount of other income received, whereas benefits from social insurance programs such as Social Security and Medicare are not.

Furthermore, program interactions are directional in that means-tested programs generally are affected by nonmeans-tested programs, but the reverse is not true. For example, some households receive benefits from both Social Security and AFDC. Changing AFDC benefits would not affect Social Security benefits, but changing Social Security benefits would affect AFDC benefits since these changes would affect the level of income on which AFDC benefits are based.

The specific ways in which benefits in one program affect benefits in another are determined by eligibility rules, benefit formulas, and program regulations. These program characteristics both influence the extent of participation in more than one program and, with a change in one program, determine the size of the increases or decreases in benefits in other programs. Although changes in one program may result in different behavior by recipients (such as work efforts) and thus affect spending in other programs, such behavioral changes only are described, but not analyzed, in this paper.

Eligibility Rules

Eligibility rules are the most basic program feature determining interactions among programs, because multiple participation can occur only if permitted by eligibility rules. In a few programs, eligibility for one program automatically confers eligibility for another. As mentioned earlier, most households receiving AFDC or SSI are categorically eligible for Medicaid. In other cases in which the primary eligibility criterion is poverty, low-income families qualify for benefits from more than one program. But, since cash assistance counts as income for means-tested programs, its receipt from one program can reduce or eliminate benefits from another.

Benefit Formulas

After the eligibility rules for more than one program are satisfied, program formulas for computing benefits are the next most important factor in determining the size of the interactions. Benefit formulas, and more specifically benefit reduction rates, determine the amount by which recipients' basic benefits are reduced as income increases. For example, in the Food Stamp Program, the fiscal year 1982 basic benefit is $233 per month for a four-person household with no income. This basic benefit is reduced 30 cents for each dollar of household income, after certain deductions have been allowed. When household income includes benefit payments from other programs, these benefits influence the amount of food stamps that a household can receive.

Benefit reduction rates are partially additive for participants in more than one program, because each program applies them to additional income. For example, in both the AFDC and Food Stamp Programs, an additional dollar earned will reduce benefits. The net benefit reduction rate is generally less than the total of the two individual rates, however, because the Food Stamp Program uses the reduced AFDC benefit to calculate the amount of food stamps beneficiaries can receive, and lower AFDC payments mean higher food stamp allotments.

Program Regulations

Program regulations, in combination with eligibility rules and benefit reduction rates, significantly influence program interactions. The two most important are the definitions of income and of the beneficiary, or "filing" unit.

Countable Income. "Countable" income is the income measure used to determine program eligibility and benefits. Rules on countable income state which benefits from other programs are included as income and which expenses for work, shelter, child care, and medical services can be deducted to obtain net countable income. If, for example, one program redefines countable income so that its benefits are reduced, benefits in other programs may increase.

Filing Unit. The filing unit is the person or group that is administratively eligible to apply for benefits. For example, filing units are the family, or subfamilies within a larger family, for AFDC; all those living together for housing assistance programs; and the individual worker for unemployment insurance. Changes in the definition of the filing unit of a cash assistance program may restrict eligibility for participants, thereby reducing the income used to set benefits in other programs.

Other Regulations. A host of other program rules and regulations either directly affect benefit levels for participants of more than one program or influence the amount of multiple participation that occurs. These rules differ considerably in various programs; among the most important rules are those defining the accounting period,[3] those for reporting income, and those for work and work registration. These definitions and regulations may increase or decrease multiple participation rates.

Changes in Recipient Behavior

A change in one program may result in changes in recipients' behavior that lead to interactions among programs. These behavioral responses include changes in rates of participation in more than one program, work effort, savings, and living arrangements (such as divorce or splitting up of households). For example, since benefit reduction rates are partially additive, participants in more than one program may have strong disincentives to work. Some evidence indicates that benefit reduction rates of 70 to 80 percent and benefits at the poverty level may result in an average of a 10 percent decline in work effort, but the results are not conclusive.[4] Because of the limited knowledge about the magnitude

---

3. The accounting period is the period of time over which a filing unit's countable income is measured to determine eligibility and benefits.

4. See Lester C. Thurow, "Equity, Efficiency, Social Justice, and Redistribution," in Organization for Economic Co-opera- (Continued)

of these effects, they are not included in the estimates presented in this paper.

MULTIPLE PARTICIPATION IN INTERACTING PROGRAMS

While the first part of this chapter discussed how eligibility rules, benefit formulas, and program regulations determine the potential amount of program interaction, this section discusses the extent to which households actually participate in more than one program.[5]

Interacting Programs for AFDC Recipients

Four programs--Medicaid,[6] food stamps, free or reduced-price school lunches,[7] and housing assistance--specifically use AFDC benefit amounts or eligibility requirements to determine their assistance levels. Therefore, changes in either AFDC benefit levels or eligibility limits could affect outlays in these four programs.

---

4. (Continued)
tion and Development (OECD), The Welfare State in Crisis (Paris, OECD: 1981); and Robert A. Moffitt and Kenneth D. Kehrer, "The Effect of Tax and Transfer Programs on Labor Supply: The Evidence from the Income Maintenance Experiments," in Ronald Ehrenberg, ed., Research in Labor Economics (Greenwich, Conn.: JAI Press, 1981). The most common effect is a reduction in the likelihood of working, rather than fewer hours worked by those who are employed.

5. This report uses the Census Bureau definition of households: they are limited to the civilian, noninstitutionalized population.

6. Some needy persons who receive Medicaid benefits, for example, those institutionalized for medical reasons and low-income elderly in nursing homes, are not represented in the data bases used in this paper, so they are not included in the estimates presented.

7. Because of limited data on participation in other child nutrition programs, only participation in the free or reduced-price lunch program of the National School Lunch Program is analyzed in this paper.

Enough AFDC families also receive benefits from these programs so that program interactions potentially could have large effects on the federal budget (see Table 1). The other programs examined in this paper have little potential for interaction with AFDC.

TABLE 1. PERCENT OF HOUSEHOLDS RECEIVING BENEFITS FROM AFDC[a] THAT PARTICIPATE IN PROGRAMS THAT INTERACT WITH AFDC

Programs that Interact with AFDC	Percent of AFDC Households Receiving Benefits from Other Programs[b]
Medicaid	100[c]
Food Stamps	75
Free or Reduced-Price Lunch[d]	55
Housing Assistance Programs[e]	19

SOURCES: CBO estimates from March 1981 Current Population Survey (CPS) and program data.

a. Aid to Families with Dependent Children.

b. Percentages cannot be added but must be considered separately.

c. All AFDC recipients are covered by Medicaid, but not all actually receive medical benefits.

d. One or more children in the household regularly eat a free or reduced-price school lunch subsidized by the National School Lunch Program.

e. Household lives in a housing unit owned by a public agency or pays reduced rent subsidized through existing housing programs of the Housing Act of 1937 (P.L. 75-412), as amended.